LOWER PERAK CO-OPERATIVE HOUSING SOCIETY BERHAD

v.

KETUA PENGARAH HASIL DALAM NEGERI

SUPREME COURT, KUALA LUMPUR
TAN SRI DATO' HARUN BIN MAHMUD HASHIM SCJ,
TAN SRI DATO' EDGAR JOSEPH JR. SCJ,
DATUK WIRA WAN YAHYA BIN PAWAN TEH SCJ
[CIVIL APPEAL NO. 01-41-91]
29 JUNE 1994

REVENUE LAW: Appeal from Special Commissioner - Onus - Primary purpose of acquiring land - Purpose ambiguous - Motive relevant - Whether motive of transaction to make profit - Trading - Whether both parties were trading.

By an agreement dated 31 July 1956, the applicant purchased an undivided 456/1043 share in a piece of land at the price of RM103,312.50. The applicants' primary object in the purchase was to develop the land, build houses thereon and sell them to members so that the applicant's objective of enabling its members to own houses is delivered. In 1968 a housing developer, Mah Poh Cheong Co. Sdn. Bhd. (the developer) entered into an agreement with the applicant, and this and subsequent agreements were formally signed to develop a portion of the said land. At all material times the developer was neither a member of the applicant nor a registered co-operative society.

However demand for houses by the applicant's members slackened due to dissatisfaction with the houses erected inspite of the applicant relaxing its rules regarding payment. As a result of the poor demand, the applicant sold 407 lots to the developer for a total price of RM495,512.50. Further the developer was allowed to retain another 41 lots.

The disposal of the 407 lots to the developer and the retention of the 41 lots by the developer gave rise to the dispute between the applicant and respondent. The applicant challenged the inclusion in its income tax assessments of sums of RM4,596.40 and RM118,994.50 representing profits received by the applicant for the disposal in 1971 of 41 lots and in 1973, of 407 lots which profits the revenue claimed to be of a revenue nature, being gains or profits from trading and therefore assessable to tax.

Held:

[1] In an appeal by a taxpayer to the Special Commissioners against an assessment made under the Act, the assessment stands unless the taxpayer is able to satisfy the Special Commissioners that the assessment is overcharged. It follows, that in such an appeal the onus is on the taxpayer to demonstrate that the assessment should not have been made and so, the assessment stands unless and until the taxpayer satisfies the Commissioners that it is wrong. The taxpayer, therefore, undertakes the same onus when he brings a further appeal to the High Court and yet another appeal to this Court.

[2] The Special Commissioners having found as a fact that the **primary purpose** of the taxpayer in acquiring the land in February 1956 was to build houses for members, that is to say, for a domestic purpose, through co-operative efforts, a finding which was amply justified by the evidence, then went on to misdirect themselves by making the wholly inconsistent finding that the acquisition of the land had **never** been treated or held as an investment and that, on the contrary, it had been held as stock in trade.

[3] When considered objectively, from the taxpayers' point of view as opposed to that of the developer, the transactions were ambiguous, in other words, their purpose would be open to two interpretations, namely, a commercial purpose or non-commercial purpose depending on how one looks at them. In such a situation, the subjective intention and therefore the motives of the parties are important factors.

[4] It is manifestly clear that the dominant purpose and also the dominant motive of the taxpayer was not to make a profit out of the transactions with the developer but to provide a roof over the heads of its members, and so, the resulting profit could not have been derived from a trading transaction or an adventure in the nature of trade but was an accretation to capital not liable to tax.

[5] By reason of the supervening events, it was the developer alone who was the participant in the trading and not the taxpayer who in desperation handed over the project to the developer.

[Applicants' appeal allowed].

[**Bahasa Malaysia** Translation of Headnote]

UNDANG-UNDANG HASIL: Rayuan daripada Pesuruhjaya Khas - Onus - Tujuan utama memperolehi tanah - Tujuan taksa - Samada motif relevan - Samada motif transaksi untuk membuat keuntungan - Perdagangan - Samada kedua-dua pihak berdagang.

Melalui suatu perjanjian bertarikh 31 Julai, 1956, pemohon telah membeli 456-1043 saham tak dibahagi dalam sebidang tanah dengan harga sebanyak RM103,312.50. Tujuan utama pemohon dalam pembelian tersebut adalah untuk membangunkan tanah tersebut, membina rumah-rumah di atasnya dan menjualkannya kepada ahli-ahli supaya objektif pemohon untuk membolehkan ahli-ahlinya memiliki rumah sendiri tercapai. Dalam tahun 1968 pemaju perumahan, Mah Poh Cheong Co. Sdn. Bhd. (pemaju) telah memasuki satu perjanjian dengan pemohon, dan perjanjian ini serta perjanjian-perjanjian yang berikutnya telah secara formal ditandatangani untuk membangunkan sebahagian tanah tersebut. Pada setiap waktu material pemaju tersebut tidak merupakan ahli pemohon atau pun sebuah pertubuhan koperasi berdaftar.

Walaubagaimanapun, permintaan untuk rumah-rumah tersebut oleh ahli-ahli pemohon menjadi berkurangan disebabkan oleh rasa tidak puas hati dengan mutu rumah-rumah yang didirikan itu walaupun pemohon telah melonggarkan peraturan-peraturannya berkaitan dengan pembayaran. disebabkan oleh permintaan yang kian menurun, pemohon telah menjual 407 lot-lot tersebut kepada pemaju dengan jumlah harga sebanyak RM495,512.50. Selanjutnya, pemaju telah dibenarkan mengekalkan 41 lot-lot yang lain.

Pelupusan 407 lot-lot tersebut kepada pemaju dan pengekalan 41 lot-lot tersebut kepada pemaju telah menyebabkan pertikaian antara pemohon dan responden. Pemohon telah mencabar kemasukan dalam taksiran cukai pendapatannya jumlah-jumlah sebanyak RM4,596.40 dan RM118,994.50 yang merupakan keuntungan yang diterima oleh pemohon bagi pelupusan tersebut dalam tahun 1971 bagi 41 lot-lot tersebut dan dalam tahun 1973 bagi 407 lot pula yang mana keuntungannya didakwa oleh Jabatan Hasil sebagai bersifat pendapatan, yang merupakan keuntungan daripada perniagaan dan dengan itu boleh ditafsirkan cukai.

Diputuskan:

[1] Dalam suatu rayuan oleh pembayar cukai kepada Pesuruhjaya Khas terhadap taksiran yang dibuat di bawah Akta tersebut, taksiran tersebut akan tetap kekal kecuali pembayar cukai tersebut dapat memuaskan hati Pesuruhjaya Khas bahawa taksiran itu adalah dicaj berlebihan. Ianya bererti bahawa dalam rayuan yang sedemikian onus (tanggungjawab) adalah ke atas pebayar cukai untuk menunjukkan bahawa taksiran tersebut tidak sepatutnya dibuat dan yang demikian, taksiran tersebut berkuatkuasa kecuali dan sehingga pembayar cukai meuaskan hati Pesuruhjaya tersebut bahawa ianya adalah salah. Pembayar cukai, dengan itu, memikul tanggungjawab yang sama apabila beliau mengemukakan rayuan selanjutnya kepada Mahkamah Tinggi dan seterusnya satu rayuan yang lain kepada Mahkamah ini.

[2] Pesuruhjaya Khas telah menentukan sebagai satu hakikat bahawa tujuan utama pembayar cukai dalam memperolehi tanah tersebut pada bulan Februari, 1956 adalah untuk membina rumah-rumah bagi ahli-ahlinya, iaitu untuk tujuan domestik, melalui usaha-usaha Koperasi, satu penemuan yang mana telah dipertahankan secukupnya oleh keterangan tersebut, kemudian seterusnya menyalah-arah diri mereka sendiri dengan membuat kesimpulan yang sesungguhnya tak konsisten bahawa pemerolehan tanah tersebut tidak pernah dianggap atau dikemukakan sebagai satu pelaburan dan bahawa, sebaliknya, ianya telah dikemukakan sebagai stok perdagangan.

[3] Apabila dipertimbangkan secara objektif, daripada pembayar cukai, bertentangan dengan pendapat pemaju, transaksi-transaksi tersebut adalah taksa, dalam erti kata lain, tujuan komersyial atau tak komersyial, terpulang kepada bagaiman seseorang itu memandangnya. Dalam keadaan yang sedemikian, niat sujektif dan dengan itu motif pihak-pihak tersebut adalah faktor -faktor penting.

[4] Ianya adalah dengan jelasnya ketara bahawa tujuan dominan dan juga motif dominan pembayar cukai adalah bukannya untuk membuat keuntungan daripada transaksi-transaksi dengan pemaju tetapi hanya untuk memberikan perlindungan atau rumah kepada ahli-ahlinya, oleh yang demikian keuntungan yang dihasilkan oleh transaksi perdagangan atau satu usaha berupa perdagangan tetapi

adalah satu penambahan keapda modal yang tidak dicukai.

[5] Disebabkan oleh peristiwa-peristiwa yang menyebabkan perubahan itu, ianya adalah hanya pemaju sahaja yang merupakan peserta dalam perdagangan tersebut dan bukannya pembayar cukai yang dalam keadaan putus asa telah menyerahkan projek tersebut kepada pemaju.

[Rayuan pemohon dibenarkan].

Cases referred to:
DGIR v. LCW [1975] 1 MLJ 250
Leeming v. Jones [1928-31] 15 TC 333
Edwards v. Bairstow & Harrison [1956] AC 14 ***(refd)***
Chua Lip Kong v. Director-General of Inland Revenue [1982] 1 MLJ 235 ***(refd)***
Lim Foo Yong Sdn. Bhd. v. Comptroller-General of Inland Revenue [1986] 2 MLJ 161 ***(refd)***
Commissioners of Inland Revenue v. Fraser 24 TC 498 ***(refd)***
Norman v. Golder 26 TC 293 ***(foll)***
The Scottish Australian Mining Co. Ltd. 81 CLR [1950] 188 ***(foll)***
Simmons v. IRC [1980] STC 350 ***(refd)***
American Leaf Blending Sdn. Bhd. v. DGIR [1950-1985] MSTC 33 ***(refd)***
Chu Lip Kong v. DGIR [1950-85] MSTC 58 ***(refd)***
Kirkham v. Williams [1991] STC 342 ***(refd)***
Ransom v. Higgs [1974] 3 AER 949 ***(refd)***
E v. Comptroller-General of Inland Revenue [1970] 2 MLJ 117 ***(refd)***
Cunliffe v. Goodman [1950] 2 KB 237 ***(refd)***
Hudson's Bay Co. Ltd. v. Stevens [1909] 5 Tax Cas 424 ***(refd)***
Inland Revenue Commissioners v. Livingstone [1926] 11 TC 538 ***(refd)***
Lupton v. FA & AB Ltd. [1972] AC 634 ***(refd)***
Coates v. Arndale Properties Ltd. [1984] 1 WLR 1328 ***(refd)***
Overseas Containers (Finance) Ltd. v. Stoker [1989] 1 WLR 606 ***(refd)***
Iswera v. Commissioners of Inland Revenue [1965] 1 WLR 663 ***(refd)***
Simmons (as liquidator of Lionel Simmons Properties Ltd.) v. Inland Revenue Commissioners [1980] 1 WLR 1196 ***(refd)***
Religious Tract and Book Society of Scotland v. Forbes [1896] 3 TC 415 ***(refd)***
Thomson v. Gurnevill Securities [1972] AC 661 ***(refd)***
Taylor v. Good [1974] STC CA 148 ***(refd)***
Rand v. Alberni Land Co. [1920] 7 TC 629 ***(refd)***
Berea West Estates (Pty) Ltd. v. SIR 38 SATC 43 ***(refd)***
Commissioners of Inland Revenue v. Reinhold 34 TC 389 ***(refd)***
Commissioners of Taxes v. British Australian Wool Realisation [1931] AC 224 ***(refd)***
Federal Commissioner of Taxation v. Whitfords Beach Property Ltd. [1978] 8 ATR 593
Stratham & Ors. v. Federal Commissioners of Taxation [1988] 20 ATR 228 ***(refd)***
Rutledge v. IRC [1929] 14 TC 490 ***(refd)***
Murray v. Commissioners of Inland Revenue 32 TC 238 ***(refd)***
Frasers (Glasgow) Bank Ltd. v. CIR 40 TC 698 ***(refd)***
Reed v. Nova Securities [1985] STC 124 ***(refd)***
Rolfe v. Wimpey Waste Management Ltd. [1989] STC 454 ***(refd)***
West v. Phillips [1958] 38 TC 203 ***(refd)***
Dunn Trust Ltd. v. Williams [1950] 31 TC 477 ***(refd)***
Page v. Pogson [1954] 35 TC 545 ***(refd)***
London County Council v. A-G [1901] AC 26 ***(refd)***

Legislation referred to:
Co-operative Societies Ordinance 1948, s. 7
Income Tax Act 1967, ss. 2, 4(a), Schedule 5 paras 34 & 35, Schedule 6 para 12(a)
Supplementary Income Tax Act 1967, s. 13(1)
Taxes Act 1970, s. 137(4) (UK)
Taxes Act 1988, s. 100 (UK)

Other sources referred to:
Halsbury Laws of England, 3rd Edn., Vol. 20, para 213, p. 119

For the appellant - C.Y. Loh; M/s. C.Y. Loh & Co.
For the respondent - Abdul Karim bin Abdul Jalil, SFC

JUDGMENT

Edgar Joseph Jr. SCJ:

Preliminary

This is an appeal from the judgment of the High Court, at Ipoh, dismissing an appeal by the Lower Perak Co-operative Housing Society Bhd. ("the taxpayer") by way of case stated by the Special Commissioners of Income Tax ("the Special Commissioners") who had dismissed its appeal against notices of assessment dated 16 August 1975 and 11 September 1982, in respect of the years of assessment 1972 and 1974, respectively.

More particularly, the taxpayer challenged the inclusion in its income tax assessments of sums of RM4,596.40 and RM118,994.50 representing profits received by the taxpayer for the disposal in 1971, of 41 subdivided building lots, and in 1973, of 407 building lots, which profits the revenue claimed to be of a revenue nature, being gains or profits from trading and therefore assessable to tax under the Income Tax Act 1967, ("the Act") and the Supplementary Income Tax Act 1967. For purposes of the assessment to income tax, the revenue considered that the proper value to be placed on the subdivided lots as stock-in-trade should be based on the cost

to the taxpayer for the land in 1956, that being the year when it acquired the land.

So far as material for purposes of the present appeal, the provisions of the Income Tax Act 1967, which it would be convenient to reproduce are as follows:

> **Section 4:** Subject to this Act, the income upon which tax is chargeable under this Act, is income in respect of:
>
> (a) gains or profits from a business, for whatever period of time.

Under para 12(a) of Schedule 6 to the Income Tax Act 1967, then applicable, the taxpayer, being a co-operative society, was exempted from income tax if the principal activities of the taxpayer consist of:

(a) transactions with its members or other co-operative societies so registered; or
(b) ...
(c) ...

The findings of fact by the Special Commissioners

The circumstances in which the sums of money aforesaid were included in the notices of assessment concerned may be taken, in substance, from the case stated, by the Special Commissioners pursuant to paras 34 and 35 of Schedule 5 to the Act, wherein they made the following findings of fact:

(i) the taxpayer is a co-operative housing society registered on 8 September 1955, under s. 7 of the Co-operative Societies Ordinance 1948;
(ii) the objects of the taxpayer as set out in by-law 3(1) of its By-laws, *inter alia* are:

(a) to buy or acquire land by purchase, mortgage, lease, exchange, gift or otherwise;
(b) to lay out land to suit the requirements of the society in the shape of roads, parks, playgrounds, schools, hospitals, markets, post offices, cinemas and other social amenities etc.;
(c) to lay out land as house sites for the benefit of the members of the society;
(d) to construct or cause to be constructed building or other works of a common utility to the society;

(e) (1) to build or cause to be built residential houses or other buildings for the members;
(2) to build houses for members on land owned by them and recover the cost thereof in instalments within a period not exceeding twenty years;
(3) to purchase land for members, build houses thereon and recover the cost in instalments within a period not exceeding twenty years;
(4) to build houses on land belonging to the society and to rent or lease them to members;

(f) to hold, sell, mortgage, lease out on hire or hire-purchase system, or otherwise dispose of land, house, house-sites, buildings and all other properties movable and immovable as may be necessary for carrying out the objects of the society; and
(g) to raise funds required for the business of the society;

(iii) in order to achieve its objects the taxpayer, by by-law 3(2), could proceed with all or any of the following:

(a) to accumulate funds by raising loans and deposits from members and non-members;
(b) to purchase, to sell, to transfer Q.T., to build, to let, to lease or to mortgage and to own movable or immovable properties like land, buildings, estates and others for the benefits of the society subject to the Ordinance & Rules made thereunder;
(c) to enter into contract with any party in order to facilitate the operations of the society;
(d) to enter into any joint venture and to establish co-operative subsidiaries; and
(e) to undertake any other activities basically proper to achieve the objects of the society;

(iv) by-law 13 and 14, application of profits and reserve fund, provide as follows:

13 (a) Out of the net profits of the society at least 25% shall be credited to the reserve fund. From the remaining net profits the general meeting shall have power to order any or all of the following payments:

(i) Gratuities to employees.
(ii) A dividend on shares not exceeding 10% on fully paid shares.
(iii) Common good fund.
(iv) Any other fund approved by the Registrar.

(b) The society may also out of the profits make allocations to any funds created by the society and approved by the Registrar. Any profits not actually disposed of in the above manner shall be carried forward to the following year.

(c) No profit shall be distributed until the accounts are audited by an auditor approved by the Registrar.

14. The reserve fund is indivisible, and no member is entitled to claim a special share in it. Until the Registrar directs that it be invested otherwise, it may be utilised in the business of the society.;

(v) on the financial year and treatment of stocks in hand, by-law 33(a) provides:

33 (a) The financial year of the society shall begin on 1 January and end on 31 December. For closing of accounts, stocks in hand shall be valued at cost price or current purchaseable price whichever is less.;

(vi) by an agreement dated 31 July 1956, the taxpayer purchased an undivided 456/1043 share in land measuring an area of 142 acres 2 roods at the price of RM103,312.50;

(vii) the taxpayer's primary object in the purchase was to develop the land, build houses thereon and sell them to members so that the taxpayer's objective of enabling its members to own houses is achieved;

(viii) the taxpayer's undivided share in the land was partitioned and it comprised three lots as follows:

(a) Lot 8265 - 116 acres 3 roods;
(b) Lot 2547 - 24 acres 0 roods 5 poles;
(c) Lot 7421 - 1 acre 1 rood 5 poles;

(ix) the taxpayer subdivided Lot 8265 into housing and shopping lots and approval was given in 1964; the application for subdivision was made immediately upon purchase of the land; individual titles for the subdivided building lots (hereinafter referred to as "the lots") were issued in 1968; the total number of lots approved for the said Lot 8265 was 787;

(x) after the approval of the subdivision of the Lot 8265 the taxpayer tried to obtain loans from more than ten financial institutions, including banks, to carry out the development of the land but was not successful; the potential lenders would not accept the taxpayer's land as security and as for guarantors which they require from the taxpayer, the financial institutions were not willing to accept committee members of the appellant ("the taxpayer") for the reason that they are subject to election every year and may not be re-elected while the loan is still outstanding;

(xi) in 1968 a housing developer, Mah Poh Cheong Co. Sdn. Bhd. ("the developer"), entered into an agreement with the taxpayer, and this and subsequent agreements were formally signed by the parties relating to the sale and development of the 787 lots comprised in Lot 8265;

(xii) at all material times the developer was neither a member of the taxpayer nor a registered co-operative society;

(xiii) (a) by an agreement dated 24 February 1968 (hereinafter referred to as "the principal agreement") the taxpayer sold to the developer a portion of Lot 8265 totalling 120 lots for the sum of RM127,191.83 i.e. at the price of RM0.25 per square foot for housing lots and RM0.625 per square foot for shop lots;

(b) by clause 6 thereof, all surveyors's fees, including the premium and cost for the issue of each of the individual titles for the 120 lots, shall be borne and paid for by the taxpayer;

(c) by clause 8 thereof, all stamp fees and solicitors' fees in relation to the agreement and the subsequent transfer shall be borne and paid for by the taxpayer;

(d) by clause 11 thereof, the developer shall have the option to purchase the balance of the lots or any portion thereof in such stages as it deems fit at the price of RM0.25 per square foot for housing lots and RM0.625 per square foot for shop lots;

(xiv) (a) by clause 1 of a supplementary agreement (A) made two days after the principal agreement, that is on 26 February 1968, the developer was obliged to sell the same 120 lots it had purchased from the taxpayer under the principal agreement, to the taxpayer's members, at a price not exceeding the price it had paid, to wit, RM0.25 per square foot, for housing lots and RM0.625 per square foot for shop lots;

(b) by clause 2 the developer shall construct for the individual purchasers of the lots such buildings on the lots in accordance with the approved layout and building plans and at a price not exceeding the price fixed by the parties;

(c) by the proviso to clause 2 the taxpayer shall be responsible for the cost of:

(1) installation of water mains reservoir and water meters,
(2) supply and installation of electrical main and substation,
(3) boundary roads,
(4) sludge pumps for septic tank,
(5) footpath/driveway from road edge to building excepting a considerated layer of sand and mining ballast, and
(6) backlanes excepting a lane of ten feet wide only;

(d) by clause 3, the taxpayer was to collect from its members the purchase price for each of the 120 lots and to retain the money as payment towards the balance of the purchase price of the said 120 lots which the developer owed the taxpayer;
(e) by clause 6 all architect's costs and fees for the building plans shall be borne and paid by the taxpayer;
(f) the taxpayer estimated the cost referred to in sub-paragraph (c) to be RM500,000;

(xv) (a) on 16 June 1969, the taxpayer and the developer made another supplementary agreement (B); by clause 1 the taxpayer shall give first priority to the developer to develop the balance of the lots in the said land;
(b) by clause 2, the houses to be built shall only be those booked/purchased by the taxpayer's members as approved by the developer's financier;
(c) by clause 6, the developer had agreed not to make any profit from the sale of the lots to members of the taxpayer; indeed, the developer had specifically undertaken to sell at cost price, that is to say, at the same price it had paid to the taxpayer;
(d) by clause 7, the taxpayer had undertaken to be responsible for the collection of the purchase price of the individual lots;

(xvi) (a) by a supplementary agreement (C) dated 25 June 1969, made between the taxpayer and the developer, the developer, had by clause 1, undertaken to carry out the development of the land until it has been fully and completely developed;
(b) by clause 2, the cost of erection of the buildings to be erected on the lots had been increased;
(c) by the proviso to clause 2, the taxpayer was to be responsible for payment of the cost of infrastructure;

(xvii) pursuant to the principal agreement and supplementary agreements (A), (B), and (C) hereinbefore mentioned, the building lots were transferred to the developer at the price of RM0.25 per square foot for housing lots and RM0.625 for shopping lots and these were subsequently resold at the same price to members of the taxpayer; the developer having entered into separate agreements with the individual member-purchasers of the taxpayer in respect of the sale and purchase of each lot and erection of a building thereon;

(xviii) the transfer of the lots by the taxpayer to the developer who had subsequently retransferred them to the individual member-purchasers of the taxpayer at the same price at which the developer had paid for each lot was to overcome the problem of raising finance for the erection of buildings on the lots by the developer;

(xix) the revenue treated the transactions in respect of the transfer of the lots to the taxpayer's members as trading transactions of the taxpayer with its members for the purposes of exemption under paragraph 12(a) of Schedule 6 to the Income Tax Act 1967;

(xx) the principal agreement read together with the supplementary agreement (A), (B) and (C) have the effect of the taxpayer selling its lots to its members;

(xxi) the transactions in the said lots were trading transactions between the appellant ("the taxpayer") and its members;

(xxii) on 25 January 1971, the appellant ("the taxpayer") and the developer entered into supplementary agreement (D) in respect of 111 lots; by clause 10, in consideration of the sum of RM95,592 to be paid by the developer to the appellant ("the taxpayer"), the appellant shall

transfer the 111 lots to the developer and it had been expressly agreed that the developer shall sell the said 111 lots only to the purchasers approved by the taxpayer at the same price at which they had been purchased by the developer from the taxpayer in the first place; the supplementary agreement (D) was supplementary to the principal agreement and supplementary agreement (A), (B) and (C);

(xxiii) however, after the signing of the supplementary agreement (D), the demand for houses by the taxpayer's members slackened due to dissatisfaction with the houses erected; inspite of the taxpayer relaxing its rules regarding payment of a deposit before booking for a lot by potential member-purchasers, 41 lots with houses built thereon out of 111 lots, were not taken up;

(xxiv) by this time the taxpayer became aware that it had to incur a lot of expenses to carry out its obligations under the agreements. The taxpayer appealed to the developer to revise the terms of the agreements but to no avail;

(xxv) the developer then informed the taxpayer that since the taxpayer could not get purchasers for the remaining 41 houses, the taxpayer had to construct the infrastructure which the taxpayer was obliged to do under the supplementary agreement (D); the appellant ("the taxpayer") estimated the cost of this to be another RM100,000. As a result, relations between the parties became strained;

(xxvi) (a) under such circumstances, the taxpayer and the developer entered into another agreement dated 1 December 1972, ("the final agreement") with regard to the disposal of the balance of 407 lots available for disposal;

(b) by clause 1 of the final agreement the appellant ("the taxpayer") sold the 407 lots measuring a total area of 1,982,950 square feet to the developer for a total purchase price of RM495,512.50, i.e. at RM0.25 per square foot;

(c) by clause 2, both parties were to be released from all the covenants and obligations under the principal and supplementary agreements entered into between them;

(d) one of the effects of clause 2 was to release the developer from its obligation to resell the remaining 41 lots (referred to in paragraph (xxiii) above) to "purchasers approved by the taxpayer" at the same price at which the developer had purchased them - the developer was thus allowed to retain the 41 lots to do what it pleased with them;

(xxvii) the explanation of the taxpayer for entering into the final agreement was as follows:

(a) it was to the advantage of the taxpayer, for it saved the taxpayer an estimated RM600,000 which the taxpayer had to spend for infrastructure pursuant to the agreements entered into between the parties. So, if the taxpayer continued with the existing agreements it would lose money;

(b) on the other hand, the final agreement would release it from all its obligations under the various agreements and the money obtained from the sale of the lots could be used for the development of another piece of land for the benefit of its members;

(xxviii) it was the disposal of the 407 lots to the developer and the retention of the 41 lots by the developer that gave rise to the dispute between the taxpayer and the revenue;

(xxix) the final agreement was a sale and purchase agreement; the release of each other's mutual obligations and rights under the previous agreements was thus part of the consideration for the sale and purchase of the said 407 lots and retention of the 41 lots by the developer;

The contentions of the taxpayer before the Special Commissioners

The Special Commissioners summarised the contentions of the taxpayer as follows:

11 (A) It was contended by the taxpayer as follows:

(i) **on the first issue** the taxpayer did not trade in land and therefore there was no business gain under the Income Tax Act; the taxpayer does not solely rely on the then exemption under paragraph 12(a) of Schedule 6 to the Income Tax Act;

(ii) the taxpayer's principal activities consisted of transactions with its members only. The revenue had confirmed it by the first paragraph of its letter dated 11 March 1982, (A2-p. 77) but added that the taxpayer had lost its tax exempt status in 1971 and 1973 when the taxpayer had entered into transaction with non-members.

(iii) if the taxpayer manages to prove that it was not trading then the onus would be discharged. The contents of the revenue's letter dated 11 March 1982, should be treated as its reasons for decision as to why, the taxpayer should be taxed, and so the revenue was barred from raising any other argument;

(iv) from the evidence, the taxpayer never changes its status as tax exempt society;

(v) the taxpayer's transactions relating to the development of the land could be split into two stages:

(a) 1st stage

2 agreements made in 1968 and

2 agreements made in 1969 (referred to as "the 4 agreements") (p. 26-39 of A2), and

(b) **2nd stage:**

2 agreements dated 25 January 1971 (p. 40 of A2) and 1 December 1972 (p. 48 of A2);

(vi) the 4 agreements (1st stage) had 3 important points:

(a) sale of subdivided lots to the developer with an undertaking by the developer to resell the same to members of the taxpayer at the same price - there was thus no resale to outsiders;

(b) these dealings had not been disputed by the revenue as the notices of assessments for years of assessment 1969 - 1971 (inclusive) had been issued and subsequently reduced to nil, and

(c) there was no actual figure in money stated in the 4 agreements although in fact money had been paid by the developer to the taxpayer; the sale of the lots to the developer who is legally obliged to resell the lots at the same price it bought from the taxpayer was a necessary device to overcome the problem of financing; but there was no change in the taxpayer's aim and object of building houses for members in an indirect form in that the taxpayer collects the money from the individual member-purchasers to satisfy the purchase price;

(vii) the dispute with the revenue arose out of the 2 agreements dated 25 January 1971 (supplementary agreement - (D) and 1 December 1972 (final agreement) - the 2nd stage of the transactions;

(viii) the supplementary agreement (D) dated 25 January 1971 relates to the sale by the taxpayer of 111 lots to the developer to be resold by clause 10, only to the purchasers approved by the taxpayer at the same price at which they were purchased by the developer in the first place; it is supplementary to and similar in nature to the 4 agreements; it was intended that only purchasers who had been invited to become, and had become members would be approved by the taxpayer to purchase the lots;

(ix) evidence showed that the developer had asked the taxpayer to look for purchasers and the taxpayer had done so but could not find purchasers for the remaining 41 lots for half a year;

(x) there was a deadlock and in these circumstances, the developer insisted upon the taxpayer carrying out its obligation under the agreements to construct the infrastructure costing about RM600,000.

(xi) the taxpayer, however, could not afford to incur the cost of RM600,000;

(xii) bearing in mind that the taxpayer would be paid RM0.25 per square foot for the 407 lots and it would at the same time be released of its obligation to construct the infrastructure, the taxpayer thought that it would be prudent to settle the matter and make the agreement dated 1 December 1972;

(xiii) before the compulsion by the developer to carry out its obligation

there had never been any intention on the part of the taxpayer to carry out any land dealing with non-members, let alone with trading;

(xiv) in reality, the agreement made on 1 December 1972 was not a sale and purchase agreement but a settlement agreement to settle their differences by releasing their obligations under the 4 agreements and supplementary agreement (D);

this was evidenced by the preamble to the final agreement which stated "And whereas both parties hereto have come to an amicable settlement of their differences...";

(xv) at the time of the final agreement the taxpayer had already covenanted to sell the 407 lots to the developer who had to resell to members of the taxpayer at the price which the developer purchased from the appellant;

(xvi) in return for the release of the liabilities and obligations of the taxpayer, the taxpayer also released the developer from selling the lots to members of the taxpayer; and the developer had to pay for the lots calculated at RM0.25 per square foot;

(xvii) the taxpayer had not deviated from its activities and objective of selling land to its members so that the so called sale in the agreements are not sale of land agreements;

(xviii) the revenue is alleging that when the taxpayer deals with members it is trading;

(xix) strictly the taxpayer, a society, means its members who control the taxpayer; the society is a collective name for members; can members trade with themselves?; can I trade with myself?; it is submitted that there is no trade in dealing with members;

(xx) even if there is trade as alleged, and a profit is made, such a profit is not profit in the real sense in that:

(a) one cannot make a profit **from** oneself, and

(b) such so called profit merely represents the refund to members;

(xxi) in this particular case members deposited money to pool their resources together to buy land for the benefit of themselves so that each member is allocated one lot of land;

(xxii) if there is some excess money left over with the taxpayer such money is not to be treated as profits, but to be refunded to members;

(xxiii) it is conceded that if members deposited money to buy land and trade and do business with third parties, then it is trading and the profit is taxable;

(xxiv) **the 2nd issue** will only arise if the Special Commissioners hold that the taxpayer was trading in land; the taxpayer relies heavily on *DGIR v. LCW* [1975] 1 MLJ 250 which decides that the cost price of the land in relation to the business in that case was the value of the land at the time of appropriation to the business in 1963 and not the original value in 1953;

(xxv) this present case is similar to the case cited except that in the taxpayer's case there was no intention to sell whereas in the case cited above there was admission of sale of 19 flats to the purchasers;

(xxvi) as submitted earlier the so called sale agreement dated 1 December 1972 is an agreement to settle differences-not a sale agreement; if the Special Commissioners are not with the appellant it is vital to determine when the sales took place i.e the commencement date of business;

(xxvii) the taxpayer submits that 1 December 1972 should be the date the taxpayer changed its purpose to trade with non-members and therefore, according to the case cited, the market value of the land as at 1 December 1972 should be taken as the cost of the land;

(xxviii) the lots are not stock-in-trade in the sense used in trading; they are members' assets purchased by members for their common use;

(xxix) the lots had always been treated as assets of the taxpayer to be used for the construction of houses for members: the word "stock-in-trade" is therefore not applicable in the taxpayer's case;

(xxx) in a way the land is an investment made by members with the eventual aim of acquiring ownership of the land by members - not for profit.

The contentions of the revenue before the Special Commissioners

The Special Commissioners summarised the contentions of the revenue as follows:

(i) the taxpayer had been trading since 1968 with members and in 1971 and 1973 with a non-member; the revenue's stand with regard to the taxpayer's taxability for the relevant years of assessment is stated in its letter dated 11 March 1982 to the taxpayer's tax consultant (A2-p. 77);

(ii) consequently the Department of Inland Revenue issued notices of assessment in respect of years of assessment 1969, 1970 and 1971 and subsequently gave a discharge by means of reduction of assessments to nil (A2-p. 71-76);

(iii) what the revenue had done by issuing the assessments and then a discharge was consonant with the view of the revenue that the taxpayer was trading with members but because it is a society, exemption was then given under paragraph 12(a) of Schedule 6 to the Income Tax Act;

(iv) whether the taxpayer is trading with members or non-members is a question of fact which the Special Commissioners must decide on the evidence before them;

(v) the taxpayer had not paid tax for any year of assessment simply because of the operation of paragraph 12(a) of Schedule 6 and not because the taxpayer is not trading;

(vi) (a) the fact that the taxpayer was trading is borne out by the evidence of its honorary secretary (AW1) who testified that the object of the taxpayer in obtaining the land was for the development of the land for members;

(b) immediately upon acquisition of the land application was made for subdivision of the land;

(c) the application for subdivision was approved in 1964 and individual titles were issued in 1968;

(d) meanwhile efforts were made to banks and financial institutions to back up the taxpayer's project;

(vii) all these efforts suggest that the taxpayer had carried on trading or made efforts to achieving its purpose from its very inception;

(viii) the objects of the taxpayer in by-law 3(1) and 3(2) of its By-laws indicate the nature and colour of the taxpayer's transactions;

(ix) that there was trading in this case is self evident; without income from trading the question of exemption does not arise;

(x) for a person to be taxed there must be income arising from any of the sources in s. 4 of the Income Tax Act; in the taxpayer's case it is trading under s. 4(a) of the Act;

(xi) the four badges of trade as explained in *Leeming v. Jones* [1928-31] 15 TC 333 were present;

(xii) the question whether there was trading has to be decided by looking at the various agreements; *prima facie* these agreements are sale and purchase agreements;

(xiii) with reference to the principal agreement dated 24 February 1968, clause 3 of the preamble to the agreement and clause 1 stated clearly the sale of 120 lots at a total purchase price of RM127,191.83; the agreement read as a whole is an outright sale of the lots from the taxpayer to the developer; the supplementary agreement (A) dated 26 February 1968 cannot modify the principal agreement;

(xiv) by clause 1 in the supplementary agreement (B), the taxpayer shall give first priority to the developer to develop the balance of the subdivided lots;

(xv) by clause 1 of the supplementary agreement (C) the taxpayer agreed to let the developer carry out the development of the land until the said land has been fully and completely developed;

(xvi) in actual fact each agreement can stand on its own;

(xvii) the taxpayer's problem started with the supplementary agreement (D) by having clauses 10 i.e. the sale of 111 subdivided lots at a price of RM95,592 to the developer who agreed to resell them to the purchasers approved by the appellant ("the taxpayer"); here again it is a sale and purchase agreement;

(xviii) the revenue had agreed with the taxpayer that the first 2 agreements read together with supplementary agreements (B) and (C) have the effect that the sale of the lots to the developer was in fact a sale of the lots to members of the taxpayer; in this respect the revenue accepted the reality of the situation;

(xix) as regards the sale of 41 lots - the balance remaining with the developer re supplementary agreement (D) - and 407 lots, there was an admission by the taxpayer in its ground of appeal that the same were regarded as having been retained by the developer who is not a member of the appellant ("the taxpayer");

(xx) Borang 14A at p. 79(a), (b), (c) and (d) of A2-4 sets of documents relating to the transfer of 49 out of the 407 lots - clearly show that the disposal was to the developer from the

appellant ("the taxpayer"); this shows an outright sale;

(xxi) the final agreement between the parties confirms that the agreement is an outright sale and purchase agreement relating to 407 lots, although the appellant ("the taxpayer") calls it a settlement agreement;

(xxii) the element of minimising the taxpayer's loss is however present in the final agreement;

2nd Issue

(xxiii) if the Special Commissioners find that the taxpayer is trading then it is pertinent to determine what is the date of trading;

(xxiv) in this respect the cost of the land - the taxpayer's stock-in-trade - should be taken to be the market value at the commencement of that trading;

(xxv) the revenue contends that the appellant ("the taxpayer") had been trading all along; if it did not trade from the date of purchase of the land then it was trading since 1968;

(xxvi) the case cited by the taxpayer in support of its 2nd issue can be distinguished from the present case and therefore should not be applied. In that case the land in question was transferred from the fixed capital account to the trading account as stock-in-trade, whereas in this case the subdivided lots (land) remained as stock-in-trade and had never been shown in the fixed capital account: see paragraph 2 at page 77 of A2;

(xxvii) also in the case cited the taxpayer was carrying on 2 businesses and therefore there was the necessity of changing the nature of the assets from fixed assets to stock-in-trade; in the present case there is only one business of housing development;

(xxviii) the taxpayer has failed to discharge its burden to prove that the assessments which have been raised against it are wrong and to what extent and in what manner they are wrong; the appeal should be dismissed and the assessments raised be confirmed.

The reply by the taxpayer before the Special Commissioners

The Special Commissioners summarised the contentions of the taxpayer by way of reply, as follows:

(i) the taxpayer cannot trade with its members;

(ii) paragraph 12(a) of Schedule 6 does not apply in this case because there was no trading at all; there was no tax payable and therefore no exemption is required;

(iii) the agreements were made between the taxpayer and the developer and not between the taxpayer and its members; therefore the contention that the taxpayer is trading with its own members is not true;

(vi) in fact all the agreement made in this case, *viz*, the principal agreement and supplementary agreement (A), (B), (C) and (D) are referred to and termed as "the development agreements" in the final agreement dated 1 December 1972; for that was the intention of the agreements i.e. to develop the land for the members;

(v) consequently, the agreements are not direct sale and purchase agreements; the taxpayer was not directly developing the land for members and therefore there was no trading between the taxpayer and its members;

(vi) as regards the case cited by the taxpayer it is the changing of the purpose of the original purchase of land from renting to sale that determined the time of commencement of business.

The questions for determination before the Special Commissioners

Having regard to the rival contentions aforesaid, the Special Commissioners considered that the principal questions for determination were as follows:

(i) whether or not the profits received by the taxpayer for the disposal of the 41 subdivided building lots in 1971 and 407 subdivided building lots in 1973 comprised in Lot 8265, constituted income in respect of gains or profits from trading and assessable to income tax under s. 4(a) of the Income Tax Act 1967 and development tax under s. 13(1) of the Supplementary Income Tax Act 1967;

(ii) if the answer to the first question is in the affirmative, whether in the ascertainment of the adjusted income of the Taxpayer from its trading for the years of assessment 1972 and 1974, the value of the stock-in-trade consisting of the said subdivided building lots should be based on the original purchase price of the land which the taxpayer paid in 1956 when it first acquired the land or whether it should be the market value at the time when the taxpayer commenced disposing of the first 120 subdivided building lots in February 1968 or whether it should be the market value at the time when the taxpayer disposed of the said 41 and 407 subdivided building lots to the developer.

The Deciding Order

In their **deciding order**, the Special Commissioners said this:

(xxx) the disposal of the said 407 and 41 lots by the taxpayer to the developer, a non-member of the taxpayer society, was trading for the purposes of s. 4(a) of the Income Tax Act;

(xxxi) the development on Lot 8265 was the only one carried out by the taxpayer;

(xxxii) unless otherwise stated, the following table shows the number of lots disposed of by the taxpayer from 1968 to 1973 to its members:

Year	No. of lots disposed of	Remarks
1968	82	-
1969	7	-
1970	151	-
1971	115	41 lots were disposed of to the developer
1972	nil	-
1973	407	all disposed of to the developer;

(xxxiii) under the then applicable paragraph 12 of Schedule 6 of the Income Tax Act, the taxpayer was exempted from income tax if the principal activities of the appellant consisted of:

(a) transactions with its members or other co-operative societies so registered; or
(b) ...
(c) ...

(xxxiv) the revenue assessed and subsequently discharged the taxpayer for the years of assessment 1969, 1970, 1971 and 1973 as follows:

Year of Assessment	Date of Assessment	Tax Payable	Date of Discharge	Amount	Tax Payable
1969	16-8-1975	$24,296.40	11-9-1982	$24,296.40	nil
1970	16-8-1975	$ 2,456.80	11-9-1982	$ 2,456.80	nil
1971	16-8-1975	$35,871.75	11-9-1982	$35,871.75	nil
1973	16-8-1975	$ 1,020.00	(not known)	$ 1,020.00	nil

(xxxv) for the years of assessment 1969, 1970, 1971 and 1973 the taxpayer was exempted from payment of tax by virtue of paragraph 12(a), Schedule 6 to the Income Tax Act;

(xxxvi) for the year of assessment 1972, by notice dated 16 August 1975, the taxpayer was assessed to tax as follows:

income tax:	RM10,241 @ 40%	RM4,096.40
development tax:	5% of RM9,304 (minimum RM500)	RM 500.00
	Total =	RM4,596.40

(xxxvii) for the year of assessment 1974 the taxpayer was assessed to tax by a notice dated 11 September 1982 as follows:

Income tax on RM272,642 @ 40%	RM109,056.80
Development tax on RM248,754 @ 5%	RM 12,437.70
Section 112(3) penalty	RM 125.00
	RM121,619.50
Tax payable as per notice dated 26 July 1975	RM 2,625.00
Additional tax payable	RM118,994.50

(xxxviii) in computing the profits on the disposal of the 407 and 41 lots the revenue took the actual acquisition price of the land acquired in 1956 as the basis for calculating its cost to the taxpayer;

(xxxix) at all material times since the acquisition of the land in 1956 the taxpayer had treated the land and, after Lot 8265 was subdivided into building lots, the lots, as stock in hand (stock-in-trade) at cost;

(xl) at all material times the said Lot 8265 and, after its subdivision, the lots comprised in it were not held as investment by the taxpayer;

The answers by the Special Commissioners

The Special Commissioners then proceeded to answer the questions aforesaid as follows:

(a) that the profits received by the taxpayer from the disposal of the 41 subdivided building lots in 1971 and the 407 subdivided building lots in 1973 constituted income in respect of gains or profits from trading and therefore were assessable to tax under the Income Tax Act 1967, and the Supplementary Income Tax Act 1967; and

(b) the proper value to be placed on the said subdivided lots as stock-in-trade should be based on the cost to the taxpayer for the land in 1956 when it acquired the land.

The question of law referred to the High Court

The Special Commissioners concluded by saying this:

> The question for the High Court is whether, on the facts found and stated by us, our decision was correct.

As the judgment of the High Court, Ipoh, merely echoes the reasoning and conclusions of the Special Commissioners, we find it unnecessary to make any reference to it except on one or two points.

The duty of the Court when hearing appeals from the Special Commissioners

First of all, it would be pertinent to say that in considering this appeal we have kept in the forefront of our minds the much quoted principles enunciated by Lord Radcliffe in *Edwards v. Bairstow and Harrison* [1956] AC 14 at 35 regarding the duty of the Court when hearing appeals from Commissioners in tax cases. It will be recalled that in that case what Lord Radcliffe said (at p. 35) was this:

> I think that the true position of the Court in all these cases can be shortly stated. If a party to a hearing before Commissioners expresses dissatisfaction with their determination as being erroneous in point of law, it is for them to state a case and in the body of it to set out the facts that they have found as well as their determination. I do not think that inferences drawn from other facts are incapable of being themselves findings of fact, although there is value in the distinction between primary facts and inferences drawn from them. When the case comes before the Court it is its duty to examine the determination having regard to its knowledge of the relevant law. If the case contains anything *ex facie* which is bad law and which bears upon the determination, it is, obviously, erroneous in point of law. But, without any such misconception appearing *ex facie*, it may be that the facts found are such that no person acting judicially and properly instructed as to the relevant law could have come to the determination under appeal. In those circumstances, too, the Court must intervene. It has no option but to assume that there has been some misconception of the law and that this has been responsible for the determination. So there, too, there has been error in point of law. I do not think that it much matters whether this state of affairs is described as one in which there is no evidence to support the determination or as one in which the evidence is inconsistent with and contradictory of the determination, or as one in which the true and only reasonable conclusion contradicts the determination. Rightly understood, each phrase propounds the same test. For my part, I prefer the last of the three, since I think that it is rather misleading to speak of there being no evidence to support a conclusion when in cases such as these many of the facts are likely to be neutral in themselves, and only to take their colour from the combination of circumstances in which they are found to occur.

In *Chua Lip Kong v. Director-General of Inland Revenue* [1982] 1 MLJ 235, Lord Diplock when delivering the unanimous judgment of the Privy Council in a tax appeal had occasion to refer, with approval, to the observations of Lord Radcliffe aforesaid in the following terms:

> ... It is plainly wrong in law; or else it is a conclusion of mixed fact and law that no reasonable Special Commissioners could have reached if they had correctly directed themselves in law. Whichever way it is looked at, it falls within the well-known principle laid down by Viscount Radcliffe in *Edwards v. Bairstow*. It is a conclusion or decision of the Special Commissioners which the High Court was entitled to and ought to have set aside.

And in *Lim Foo Yong Sdn. Bhd. v. Comptroller-General of Inland Revenue* [1986] 2 MLJ 161, when delivering the unanimous judgment of the Privy Council, Lord Oliver, indicated in what circumstances, a Court might interfere with the decision of the Special Commissioners. Here is what his Lordship said (at p. 169, col 2 F to H):

> The Special Commissioners are, of course, as the Federal Court rightly observed, the Judges of fact, but in finding the facts and drawing inferences of secondary fact from them, they must not misdirect themselves and they must draw conclusions from facts having probative value. In their Lordships' judgment, the Special Commissioners in this case both misdirected themselves by reaching conclusions inconsistent with primary facts found by them and drew inferences from matters which were of no probative value in supporting their conclusions.

In *Commissioners of Inland Revenue v. Fraser* 24 TC 498, Lord President Normand said this (at p. 501):

> Then the Commissioners, on consideration of the facts and arguments submitted to them, decided by a majority that an adventure in the nature of trade had not been carried on; that an investment had been made and subsequently realised, and that the profit was not assessable

to income tax. It is obvious from the way in which the Commissioners have stated their conclusion that they were quite aware that they were not stating something in the nature of a primary fact but were stating a conclusion into which argument upon the construction of the Income Tax Act had entered. The respondent's Counsel maintained, however, that that finding was a finding in fact and, as such, was not reviewable by this Court. I think we have jurisdiction to entertain the question at law, which is whether the majority of the Commissioners were warranted on the evidence in determining as they did. At the narrowest it is always open to this Court in a stated case to review a finding in fact on the ground that there is no evidence to support it. That has been stated again and again.

The onus on the taxpayer

We recognise that in an appeal by a taxpayer to the Special Commissioners against an assessment made under the Act, the assessment stands unless the taxpayer is able to satisfy the Special Commissioners that the assessment is overcharged. It follows, that in such an appeal the onus is on the taxpayer to demonstrate that the assessment should not have been made, (see *Norman v. Golder* 26 TC 293, per Macnaghten J. at p. 295) and so, the assessment stands unless and until the taxpayer satisfies the Commissioners that it is wrong (per Lord Greene MR at p. 295). The taxpayer, therefore, undertakes the same onus when he brings a further appeal to the High Court and yet another appeal to this Court.

Before us the decision of the Special Commissioners was attacked on a number of grounds.

Inconsistent findings of fact

The first ground of appeal which we should like to consider is the taxpayer's contention that the Special Commissioners had erred in law in that after having found as a fact - with serious legal consequences - that the taxpayer's **primary object** in the purchase of the land was to develop the land, build houses thereon and sell them to members, so that the taxpayer's objective of enabling its members to own houses is achieved, went on to arrive at the unreasonable and contradictory conclusion that the land since the date of acquisition had never been treated or held as an investment of the taxpayer; on the contrary, it was held as stock-in-trade throughout.

It is unnecessary to discuss the evidence at any length and, it will suffice, if we say, that the Special Commissioners finding of fact that the taxpayer's primary object in the purchase of the land was to develop it, build houses thereon and sell them to its members, was amply justified by the evidence and, indeed, was unassailable.

The Special Commissioners had made it unmistakably clear in their case stated that at the time of the purchase of the land the aim of the taxpayer was to build houses for its members. In so holding, the Special Commissioners had drawn an inference from a scrutiny of the taxpayer's by-laws.

True it is that the by-laws are not conclusive of a society's intention as much as the memorandum of association is not conclusive of the intention of a company. (See *The Scottish Australian Mining Co. Ltd.* 81 CLR [1950] 188). But, when as here, the principal objects of the taxpayer are implemented, as indeed had been found by the Special Commissioners (see finding (vii)) then this, of course, supports the contention of the taxpayer that it had no intention to trade at the time of acquisition of the asset. To put it another way, it supports the contention of the taxpayer that it had no intention, at the time of the acquisition of the asset, of disposing of it at a profit, but rather that the asset was acquired as a permanent investment. In support of this contention the following passage in the judgment of Lord Wilberforce in the House of Lords case of *Simmons v. IRC* [1980] STC 350 at 352 was cited:

> One must ask, first, what the commissioners were required or entitled to find. Trading requires an intention to trade: normally the question to be asked is **whether this intention existed at the time of acquisition of the asset. Was it acquired with the intention of disposing it at a profit or was it acquired as a permanent investment?** Often it is necessary to ask further questions: a permanent investment may be sold in order to acquire another investment thought to be more satisfactory; that does not involve an operation of trade **whether the first investment is sold at a profit or at a loss.**
> (Emphasis supplied)

Clearly, therefore, the Special Commissioners having found as a fact that the **primary purpose** of the taxpayer in acquiring the land in February 1956 was to build houses for mem-

bers, that is to say, for a domestic purpose, through co-operative efforts, a finding - we would interpolate to repeat - which was amply justified by the evidence, then went on to misdirect themselves by making the wholly inconsistent finding that the acquisition of the land had **never** been treated or held as an investment and that, on the contrary, it had been held as stock-in-trade.

True also it is that whether a taxpayer carries on a business is a question of fact but when, as here, there is a misdirection, it becomes "a conclusion of law". (See *American Leaf Blending Sdn. Bhd. v. DGIR* [1950-1985] MSTC 33 at p. 37; *Chu Lip Kong v. DGIR* [1950-85] MSTC 58, 63, Privy Council).

It is clear law that where the Special Commissioners have misdirected themselves by reaching conclusions inconsistent with the primary facts found by them this could lead to a reversal of their decision; in other words, the mere fact that the Special Commissioners have made a finding of fact is not conclusive of the matter. It is not difficult to cite an anthology of cases in support of this proposition. Our choice is as follows.

In *Lim Foo Yong Sdn. Bhd. (ibid)* the Special Commissioners having found, *inter alia*, as a fact that capital had been raised to expand the hotel business, then went on to hold that transactions designed for this purpose had given rise to taxable income simply because something - namely, land and shares, - had been bought and sold at a profit. It was held by the Privy Council that in relation to the company reconstruction effected by the transfer of the benefit of the repurchase agreement and the exchange of the Merlin Shares for those in the hotel company, the Commissioner's decision was inconsistent with their finding that the taxpayer company's purpose was the further expanding of the business. The taxpayer's appeal, therefore, succeeded and the assessments discharged.

In *Simmons v. IRC*, the Special Commissioners having found that the intention of the Simmons group of taxpayer companies was "primarily for the purpose of creating and retaining investments" (at p. 354 - g), then went on to make the inconsistent finding that the intention was also to trade where investment was not possible. It was held by the House of Lords that one could not trade and, at the same time invest although there could be change of intention. Furthermore, the House held that the Commissioners' reference to the group's original aim to create investment for retention where possible, or where not possible for turning to account by way of trade, itself not a finding of fact, was inconsistent with the whole history of the group and with their clear finding that the initial intention of the group was "primarily for the purpose of creating and retaining the investments (and) not... for the purpose of immediate sale after development". The House concluded that on the facts the sale of the properties in question was not a sale in the course of trade, but a realisation of capital and accordingly allowed the taxpayer's appeal.

In *Kirkham v. Williams* [1991] STC 342 at 355j to 356a, Lord Justice Lloyd said:

> ... I am satisfied that the Commissioners have erred in law. Their conclusion is inconsistent with their primary finding of fact.

The critical question for the determination of this Court

That, however, is not the end of the matter, for intentions may be changed, and so the specific question of critical substance is: whether when between 1969 and 1972 the taxpayer had entered into the three related transactions with the developer (a non-member as evidenced by the contemporary agreements hereinbefore mentioned), it had engaged in a trade or an adventure in the nature of trade. We are supported in this by what the Privy Council said in *Lim Foo Yong Sdn. Bhd.*, namely, that what was vital was the intention of the taxpayer and whether the intention remained the same.

What is trading?

This brings us to the question: what is trading?

In *Ransom v. Higgs* [1974] 3 AER 949 Lord Reid said (at p. 955):

> The Income Tax Acts have never defined trade or trading farther than to provide that trade includes every trade, manufacture, adventure or concern in the nature of trade. As an ordinary word in the English language 'trade' has or has had a variety of meanings or shades of meaning. Leaving aside obsolete or rare usage it is sometimes used to denote any mercantile operation but it is commonly used to denote operations of a commercial character by which the trader provides to customers for reward some kind of goods or services. As there

is no limit defining trade it has been held to include cases where some element is absent which is normally present in trading.

In *E v. Comptroller-General of Inland Revenue* [1970] 2 MLJ 117 at 122 col 1 H and I: Gill FJ speaking for the Federal Court said this:

> Whilst a trade usually consists of a series of transactions implying some continuity and repetition of acts of buying and selling or manufacturing and selling, in view of the definition of 'trade' in the English Income Tax Act which I have mentioned above, the mere fact that there is only one transaction does not preclude the possibility that that transaction is in the nature of a trade. (Thus, one single purchase and sale or one purchase and many sales have been held in the English and Scottish Courts to be trading (see **Halsbury**, 3rd Edn., Vol. 20, paragraph 213, page 119).

In *Simmons v. IRC (ibid)* at 1197, Lord Wilberforce answered the question "what is trading?" in the following passage, part of which we have earlier reproduced:

> One must ask, first, what the Commissioners were required or entitled to find. Trading requires an intention to trade: normally the question to be asked is whether this intention existed at the time of the acquisition of the asset. Was it acquired with the intention of disposing of it at a profit, or was it acquired as a permanent investment? Often it is necessary to ask further questions: a permanent investment may be sold in order to acquire another investment thought to be more satisfactory; that does not involve an operation of trade, whether the first investment is sold at a profit or at a loss. Intention may be changed. What was first an investment may be put into the trading stock, and, I suppose, *vice versa*. If findings of this kind are to be made precision is required, since a shift of an asset from one category to another will involve changes in the company's accounts, and, possibly, a liability to tax (of *Sharkey (Inspector of Taxes) v. Wernher* [1956] AC 58, 36 TC 275). What I think is not possible is for an asset to be both trading stock and permanent investment at the same time, nor to possess an indeterminate status, neither trading stock nor permanent asset. It must be one or other, even though, and this seems to me legitimate and intelligible, the company, in whatever character it acquires the asset, may reserve an intention to change its character. To do so would, in fact, amount to little more than making explicit what is necessarily implicit in all commercial operations, namely that situations are open to review.

In *Cunliffe v. Goodman* [1950] 2 KB 237 at 253, Lord Asquith speaking about what in law amounts to an intention said this:

> An intention to my mind connotes a state of affairs which the party "intending" - I will call him X - does more than merely contemplate: it connotes a state of affairs which, on the contrary, he decides, so far as in him lies, to bring about, and which, in point of possibility, he has a reasonable prospect of being able to bring about by his own act of volition... X cannot... 'intend' a result which is wholly beyond the control of his will.

And at p. 254, paras 2 & 3, his Lordship added this:

> This leads me to the second point bearing on the existence in this case of 'intention' as opposed to mere contemplation. Not merely is the term 'intention' unsatisfied if the person professing it has too many hurdles to overcome, or too little control of events: it is equally inappropriate if at the material date that person is in effect not deciding to proceed but feeling his way and reserving his decision until he shall be in possession of financial data sufficient to enable him to determine whether the project will be commercially worthwhile.
>
> A purpose so qualified and suspended does not in my view amount to an 'intention' or 'decision' within the principle. It is mere contemplation until the materials necessary to a decision on the commercial merits are available and have resulted in such a decision.

And, then, having touched on the facts before him, his Lordship also said this:

> Neither project moved out of the zone of contemplation - out of the sphere of the tentative, the provisional and the exploratory - into the valley of decision.

Does subdivision of land signify trading?

At this point, it would be convenient if we turn to consider the topic of subdivision. It is obvious that subdivision of land does not *per se* signify trading. It is necessary to enquire what was the purpose of the subdivision. It goes without saying, that if the subdivision was done for the purpose of rendering land more saleable for the purpose of trading then he who does so, does so not as owner but as a land speculator. By the same token, if the subdivision was done in furtherance of a co-operative society's aim of pooling its financial resources of all its members and, with it, to purchase a plot of land with a view to satisfying their domestic need of each

having a roof over his head, then this would not necessarily signify a badge of trading.

In the *Scottish Australian Mining Co.* case *(ibid)*, a company had been formed not for the purpose of profit but primarily for mining. In the course of winding up its mining operations, it embarked upon subdivision and sale of subdivided lots. It was held that the subdivision and sale of the subdivided lots did not constitute stock-in-trade but the realisation of a capital asset.

In the *Hudson's Bay Co. Ltd. v. Stevens* [1909] 5 Tax Cas. 424, Farwell LJ said at p. 437 that:

> A land owner may lay out part of his estate with roads and sewers and sell it in lots for building, that he does this as an owner, not as a land speculator... It would be different if a land owner, an individual, entered into the business of buying and developing and selling land; but the case of the owner, whether of land, or pictures, or jewels, selling his own property, although he may have expended money on them in getting them up for sale, is entirely different; he sells as owner, not as trader.

So, we must ask ourselves whether regard being had to the facts and circumstances proved or admitted in this case, the inference drawn by the Special Commissioners, that the relevant transactions entered into by the taxpayer with the developer were an adventure or concern in the nature of trade was justified.

In other words, before us, the broad question for decision, is whether on the facts found by the Special Commissioners, they were entitled to arrive at the decision at which they did. Such a question, as the authorities cited plainly show, raises a point of law and is within our jurisdiction to entertain in an appeal by way of case stated.

The Guiding Principles

Before embarking upon a consideration of the specific question of critical substance aforesaid, there are certain well established principles which need to be kept in the forefront of our minds and they are as follows:

The form of the documentation and the terms thereof

Generally, when considering the question whether a particular transaction to which a taxpayer is a party constitutes a trading transaction, the Court would, first of all, have to consider, objectively, whether the transaction has the outward appearance of trading transactions or, in other words, whether the documents and terms thereof were normal when compared to transactions of the like kind in the commercial world and carried out in a similar way. (See *Inland Revenue Commissioners v. Livingstone* [1926] 11 TC 538, 542 per Lord Clyde).

Paramount object of transaction: Does it have a commercial purpose?

In *Lupton's* case [1972] AC 634, at 660 C Lord Glaisdale's statement that if the appearance of the transaction leaves the matter in doubt, an examination of its *paramount object* will always be relevant and will generally be decisive, indicates that there can be cases where despite the commercial features of a transaction, if its object is fiscal, then that would be decisive. This means that the prospect of profit is not conclusive.

Secondly, even if a transaction has all the attributes of trade it must still have a commercial purpose (See e.g. *Lupton v. F.A. & A.B. Ltd.* [1972] AC 634; *Coates v. Arndale Properties Ltd.* [1984] 1 WLR 1328, 1333; *Overseas Containers (Finance) Ltd. v. Stoker* [1989] 1 WLR 606, 613).

Subjective Intention and Motive of the Parties

In determining the question whether a transaction has a commercial purpose or object the subjective intention of the parties to it may be material; it would be material if the transaction is ambiguous or, in other words, its purpose were open to two interpretations namely, a commercial purpose or a non-commercial purpose. When the subjective intention of the parties becomes a relevant factor, the motives of the parties may be most material. We need hardly add that there is a fundamental difference between intention and motive; intention means seeking to do something and is connected to purpose or object whereas motive is concerned with the reason for doing something.

It has been said that motive may be of considerable importance in borderline cases.

In *Iswera v. Commissioners of Inland Revenue* [1965] 1 WLR 663, a taxpayer had wished to reside near the school which her daughters were attending and with this in mind she had bought a $2\frac{1}{2}$ acre plot which she had subdivided into 12 building lots, nine of which she had sold to nine

sub-purchasers keeping one for her own house and two for re-conveyance to the vendor. The question for determination was whether on the facts the inference that the transaction was an adventure or concern in the nature of trade was justified. Speaking for the judicial committee of the Privy Council, Lord Reid said this at p. 668:

> If ... the taxpayer has to embark on an adventure which has all the characteristics of trading, his purpose or object alone cannot prevail over what he in fact does. But if his acts are equivocal his purpose or object may be a very material factor when weighing the total effect of all the circumstances.
>
> In the present case not only has it been held that the appellant's dominant motive was to make a profit, but her actions are suggestive of trading as regards the greater part of the site which she bought. She had to and did make arrangements for its subdivision and immediate sale to the nine sub-purchasers before she could carry out her contract with the vendor of the site.

The intention, and consequently the motive of the taxpayer, can be relevant to the question of trade or investment where the transaction is ambiguous, as for example, the purchase and sale of assets which are capable of being investment. (See Simmons (as liquidator of *Lionel Simmons Properties Ltd. v. Inland Revenue Commissioners* [1980] 1 WLR 1196).

In *Religious Tract and Book Society of Scotland v. Forbes* [1896] 3 TC 415, the society had been established for the distribution of religious literature sent out colporteurs who sold Bibles and acted as cottage missionaries. The colporteurs would travel selling their wares from door to door for the purpose of administering religious advice to customers with a view to spreading the gospel. The society also sold Bibles at a shop; the shop showed a profit, but the colportage a loss. The colporteurs would appear to have carried on a business by sale and purchase. Nevertheless, it was held that the selling of the Bibles did not constitute trading since the object of the colporteur was missionary work by engaging the customer in religious discussion with a view to spreading the gospel and so the loss could not be set off against the profits.

One party to a transaction may be trading but not the other

Next, in regard to a particular transaction, one of the parties thereto may be trading yet the other may not. Take the case of an ordinary land owner who sells a plot of land which he acquired by purchase without present intention to sell, later sells it to a property developer at a profit, no one would doubt that the former is not trading but that the latter is. This is because the former sells as land owner not as land speculator. The nature of the transaction must be determined from the point of view of the taxpayer. (See *Lupton's* case, at p. 654 C per Viscount Dilhorne at p. 654 C and *Thomson v. Gurnevill Securities* [1972] AC 661, at p. 678 B per Lord Simon of Glaisdale.)

It is with the above principles in mind that we turn to consider the question of critical substance aforesaid.

We must now identify the precise nature of the three related transactions hereinbefore mentioned which the taxpayer entered into with the developer as evidenced by the contemporary agreements particularised in the case stated.

What form did the relevant transactions take and what were their terms?

We must first consider the form which the relevant transactions took as evidenced by the relevant agreements entered into by the taxpayer and the developer. This appears sufficiently from the facts appearing in the case stated to which we have made extensive reference and we do not propose to repeat them. Suffice it to say, that we do not consider that the relevant agreements and the terms thereof were normal when compared to transactions of the like kind in the commercial world, nor carried out in a similar way, given the history of the matter.

Take for example, the important provisions as to pricing; these were based not on a profit making operation but on certain financial terms agreed to by the developer and referred to by the Special Commissioners in their finding at para (xv)(c) of their case stated which reads as follows:

> (c) by clause 6, the developer agreed not to make any profit on the land by selling the lots to members of the appellant ("the taxpayer") at the same price per square foot it purchased from the appellant ("the taxpayer").

The Judge did himself advert to the pricing aspect of the relevant agreements, but not **the significance** thereof, in the context of this part

of the argument advanced on behalf of the taxpayer. What he said was this:

> The said 407 lots were sold, not at the market price, but at the old price of 25 cents per sq. ft.; the market value having been found and stated by the Special Commissioners to be RM1 per sq. ft.

It seems to us, therefore, that Counsel for the taxpayer had considerable justification for posing the question: "Is this the attitude of persons embarking on a trading venture?"

Accordingly, we would answer the question as to the form which the relevant transactions took, in particular, whether they were normal when compared to transactions of the like kind in the commercial world and whether they were carried out in a similar way, in favour of the taxpayer, that is to say, in the negative.

Did the relevant transactions have a commercial purpose?

The next question we must consider, having regard to the authorities cited is whether the relevant transactions entered into by the parties had a commercial purpose or object **from the taxpayer's point of view** as opposed to that of the developer, and this would make the taxpayer's intention and therefore its motive relevant. Non-commercial motivation may so affect the nature of trading transactions that they cease to be normal trading transactions. (See *Religious Tract and Book Society of Scotland v. Forbes (ibid)).*

It is obvious that a mere sale at a profit is not a trading activity.

Indeed, we consider that it would be wrong to assume that in every case where a landowner enters into a transaction with a housing developer, the landowner would be embarking on an adventure in the nature of trade. We are supported in this by the following passage in the judgment of Lord Justice Russel speaking in the Court of Appeal in *Taylor v. Good* [1974] STC CA 148 at p. 154 - h and i:

> All these cases, it seems to me, point strongly against the theory that a man who owns or buys without present intention to sell land is engaged in trade if he subsequently, not being himself a developer, merely takes steps **to enchance the value** of the property **in the eyes of a developer** who might wish to buy for development.
> (Emphasis provided).

Taylor v. Good, was followed in *Rand v. Alberni Land Co.* [1920] 7 TC 629 where a number of persons who owned land had floated a company merely as machinery to realise their interests in that land. Expenditure had been incurred by the company in clearing the land and putting in roads and procuring a railway company to bring in a line to open up the area. The Court held that this was merely enhancing the value of the land and not trading.

Similarly, in the Australian case of *Scottish Australian Mining Company Ltd. (ibid),* a company was held to be merely enhancing the value of its asset although it had carried out wholesale works on its land by way of subdivision of the land, the construction of roads, the preparation of site plans for schools and churches, setting aside land for schools and churches, for parks and the construction of a railway station.

So also, in the South African case of *Berea West-Estates (Pty) Ltd. v. SIR 38 SATC 43,* although a taxpayer company with the intention of realising its land had subdivided it, installed water and electricity, made and repaired roads and carried out surveys; this work being done to render the land more saleable, was held not to be trading.

Then, again, in considering the question whether there had been an intention to trade a factor to which regard may be had is the nature of the subject matter in question; more particularly, whether the subject matter is *prima facie* an investment. Thus, in *Commissioners of Inland Revenue v. Reinhold* 34 TC 389 at p. 393, Lord Carmont said this:

> A disclosed intention not to hold what was being bought might, as Lord Dunedin said, provide an item of evidence that the buyer intended to trade and if the commodity purchased in the single transaction was not of a kind normally used for investment but for trading and if the commodity could not produce an annual return by retention in the hands of the purchaser, then the conclusion may easily be reached that the adventure was a trading one. If, however, the subject matter of the transaction is normally used for investment - land, houses, stocks and shares - the inference is not so readily to be drawn from an admitted intention in regard to a single transaction to sell on the arrival of a suitable pre-selected time or circumstances and does not warrant the same definite conclusion as regards trading or even that the transaction is in the nature of trade.

It was submitted for the revenue that the transactions entered into by the taxpayer with the developer had the characteristics of a commercial operation. In support of this submission our attention was directed to the following facts: By reason of the low quality of the buildings constructed, there were no buyers amongst the taxpayer's members in respect of the 41 lots (being the balance of the 111 lots). So, pursuant to the relevant agreement, the taxpayer had sold those 41 lots to the developer together with the 407 lots.

After setting off the purchase price of the land being Lot No. 8265, which was owed by the developer to the taxpayer, the balance was paid to the developer. The result was that the taxpayer got the purchase price of the lots sold with a profit.

This submission reflects the reasoning of the Special Commissioners when they said "whatever the terms and conditions in the final agreement were the reality of the transaction in its totality resulted in the disposal of the subject lots in dispute to the developer at a profit to the appellant ("the taxpayer") and this is the crux of the matter for tax purposes." And, indeed, the Judge, too, said that he could not quarrel with this reasoning of the Special Commissioners.

Clearly, in drawing the inference that the relevant transactions entered into by the taxpayer and the developer were an adventure or concern in the nature of trade the Special Commissioners did not apply the principles to be distilled from the various authorities to which we have referred but instead adopted an over-simplistic approach; namely, by saying that the crux of the matter for tax purposes was whether there was a disposal of the subject lots at a profit.

Understandably, therefore, it was submitted by Counsel for the taxpayer in reply, that the Special Commissioners had been unduly influenced by the fact that an organisation, to wit, a co-operative society, had been set up to organise things and that a gain had been made on the disposal or realisation of subdivided land to the developer, a non-member of the taxpayer. As a result, it was urged that the Special Commissioners had overlooked or failed to take into account the following factors:

(1) the element of intention or motive of the taxpayer at the time of acquisition of the land and the legal significance thereof; the intention or primary purpose being to satisfy the need for a roof over one's head. Since the taxpayer was a co-operative society the purpose was to pool the financial resources of all the members and with the combined sum to purchase the land.

(2) that a co-operative society had to incorporate itself under the Co-operative Societies Act 1948.

(3) that subdivision of land by a landowner is a neutral fact, and

(4) that the sale of the lots concerned by the taxpayer to the developer was in a sense, a forced sale.

Counsel for the taxpayer derived support for the proposition aforesaid from the cases of *Scottish Australian Mining Co. Ltd. (ibid)* and *Commissioners of Taxes v. British Australian Wool Realisation* [1931] AC 224.

In the *Scottish Australian Mining Co.* case *(ibid),* the taxpayer company had been formed "primarily" and "essentially" for the purpose of mining. It had purchased lands for this purpose although it did not appear to be carrying on mining for this purpose but it did carry on coal mining on a large piece of land, "the Lambton Freehold Estate" (Lambton Estate). After the coal seam was exhausted, the taxpayer commenced to subdivide the Lambton Estate and sell the subdivided lots in a big way. A small portion was set aside for homes for the miners but the rest were for commercial sale made attractive by the building of roads, a railway and lots were sold or granted for the building of churches, schools and hospitals and the provision of parks.

Williams J. after observing that the mining company was not formed for the purpose of trade, went on to consider, *inter alia,* whether the sale of the land by it constituted a trading activity. In considering this question, his Lordship asked himself the following question:

"Was the purchase made with the intention of selling at a profit? (at p. 194 bottom)." He concluded that the mining company was merely realising a capital asset and not disposing of stock in trade. In so concluding, he made the following findings and/or enunciated the following principles:

(i) it (the land) was purchased with the intention of carrying on coal mining; see bottom of p. 194; therefore it was not trading; **P. 195, middle;**

(ii) subdivision of the land did not necessarily make it stock in trade: "... it was land which because of its locality and size could only be sold to advantage in subdivision ..." **P. 195, lower middle;**
(iii) the taxpayer company was not formed for the purpose of trading this being one of the factors to take into account; **p. 192, bottom;**
(iv) merely realising property is not trading; the act and purchasing and reselling must be taken into account; **p. 196, middle.**

And, at p. 196 Williams J. said this:

> A landowner may lay out part of his estate with roads and sewers and sell it in lots for building so that he does this as **an owner** not as a land speculator ... There is also the statement of Rowlatt J. ... that 'in order to see clearly that the *Hudson's Bay* case for instance does not apply, there must be something in the nature of buying at any rate, and not merely selling, which is mere turning your property into money'.

And, at p. 252 his Lordship's statement that "merely realising is not trading. It is no good saying that it is a trade of realising ... so that in the course of carrying on a trade they have in fact done some realising", was supported by the Privy Council in *Commissioners of Taxes v. British Australian Wool Realisation (ibid* at p. 252) wherein the Privy Council said that the mere extensiveness of the organisation set up to realise an asset or assets does not of itself cause the realisation to become a business. Lord Blanesborough, speaking for the Privy Council said that was a "proposition not to be entertained."

We are aware that in the later Australian case of *Federal Commissioner of Taxation v. Whitfords Beach Property Ltd.* [1978] 8 ATR 593 the decision of Williams J in *Scottish Australian Mining Co.* case was doubted by two Judges of the High Court of Australia (namely, Mason J. and Wilson J.). Nevertheless, the principles as opposed to the decision of Williams J. in the *Scottish Australian Mining* case were affirmed by the Federal Court of Australia in *Stratham & Ors. v. Federal Commissioners of Taxation* [1988] 20 ATR 228.

But, more importantly, in *Lim Foo Yong Sdn. Bhd.* the Special Commissioners had, as had the Special Commissioners in the present case, erred in holding that the mere acquisition and sale of an asset resulting in a profit constitutes trading or an adventure in the nature of trade. Here we should like to refer to the headnote to *Lim Foo Yong Sdn. Bhd.* [1986] STC at p. 255) which reads as follows:

> The Special Commissioners, in spite of having found, *inter alia* that capital had been raised to expand the hotel business, upheld the assessments. **They had assumed that, since the objects of the taxpayer company enabled it to trade in land or shares, it followed inexorably that, if it had once acquired land and sold shares at a profit, it was to be labelled as a company engaged in the business of dealing in property and that all its property, for whatever purpose held, necessarily constituted trading stock, the profitable disposition of which would give rise to a trading profit.**

The Privy Council stressed that what was vital was the intention of the taxpayer and whether that intention remained the same or had changed.

The profit motive

The presence or absence of an intention to make a profit can be a cogent factor in deciding whether on the facts the transaction is invested with the character of trade.

So, for example, in *Rutledge v. IRC* [1929] 14 TC 490, the appellant who was interested in a cinema company had purchased one million rolls of toilet paper in a single lot and re-sold it at a vast profit.

The appellant's appeal was dismissed and Lord President Clyde giving the reasons for the Court's decision (at p. 496) said this:

> An adventure it certainly was; for the appellant made himself liable for the purchase of this vast quantity of toilet paper obviously for no other conceivable purpose than that of reselling it at a profit; and that is just what he did. The element of adventure accordingly entered into the purchase from the first. It has been said, not without justice, that mere intention is not enough to invest a transaction with the character of trade. But, on the question whether the appellant entered into an adventure or speculation, the circumstances of the purchase and also the purchaser's object or intention in making it, do enter, and that directly, into the solution of the question.

The significance of the subject matter of the transaction and its determining effect was described by Lord Sands (at p. 497) in the following words:

> The nature and quantity of the subject matter dealt with exclude the suggestion that it could

have been disposed off as otherwise than a trade transaction.

It was further submitted for the revenue that the sale of trading stock in difficult or hard pressed situation does not change the character of trading stock or trading activities. In support, our attention was directed to *Murray v. Commissioners of Inland Revenue* 32 TC 238 and *Frasers (Glasgow) Bank Ltd. v. CIR* 40 TC 698.

In *Murray's* case the overriding consideration was that the appellant was a timber merchant and it was this which led the Court to hold that there was no reason for treating the appellant differently from any other timber merchant or for treating the transactions concerned as anything but the commercial disposal of a quantity of standing timber by a timber merchant and **not** the realisation of his rights as a capital transaction the profits of which were not assessable to tax.

In *Fraser's* case the issue for determination was whether the surplus arising upon the sale of one of the company's holdings of shares, to wit, £4,314 5s, non-voting stock, in House of Fraser Ltd., was a profit of the company's trade of banking or a profit on capital account. It was in evidence that the shares concerned had been originally purchased by the company because its Chairman and Managing Director Sir Hugh Fraser who owned virtually all its share capital, had decided to support the market, in the price of this stock by buying it. The shares had been held for some years and were sold upon a demand by the company's bankers that its overdraft with them should be reduced.

The company had sought to assimilate the situation to that of an ordinary individual realising a capital investment to repay an overdraft. But it was held that the company's trading set-up could not be equiparated to that of an ordinary individual, and that accordingly the question of law should be answered in favour of the revenue. (per the Lord President Clyde at p. 704 para 5).

Neither *Murray's* case nor *Fraser's* case are authorities for the proposition for which they were cited.

Nor, for that matter, does the proposition advanced on behalf of revenue that the sale of trading stock in difficult or hard pressed situation does not change the character of trading stock or trading activities, assist the revenue because in the present case, what is also **in dispute** is whether the subject matter of the disposal by the taxpayer to the developer, to wit, the lots concerned, were, trading stock and also whether the taxpayer was, at the material time, engaged in trading activities or activities which could be described as an adventure in the nature of trade.

Asset enhancement and stock in trade

We have already noted from the authorities cited, that merely improving the value of land by clearing it, carrying out all necessary surveys, subdividing it, constructing roads, drains, installing water and electricity to render it saleable (or more saleable) in regard to a single transaction to sell at a suitable pre-selected time or in certain circumstances, does not warrant the same definite conclusion as regard trading or even that the transaction is in the nature of trade. (Per Lord Carmont in *Commissioners of Inland Revenue v. Reinhold, ibid).* In such a situation, in no sense does the land become part of the raw materials of trade, namely, trading stock.

The Special Commissioners had held that the land was held as stock-in-trade because the taxpayer was trading. True it is that if the taxpayer had been trading then the asset would be stock in trade and its sale or realisation at a profit would yield proceeds of an income nature liable to be brought into the computation of income tax. But if, on the other hand, the taxpayer had **not** been trading, then the asset would have been of a capital nature and its sale or realisation at a profit, would have been a capital gain not liable to be brought into the computation of income tax.

It follows that whether or not the lots disposed of by the taxpayer to the developer were stock in trade depends on whether it can be established that the taxpayer was, at the material time, trading or been engaged in an adventure in the nature of trade. That is the key question. We are fortified in this view, by a consideration of the definition of stock in trade appearing in s. 2 of the Act, which reads:

> 'stock in trade' in relation to a business, means property of description, whether movable or immovable being either -
>
> (a) property such as is sold in the ordinary course of the business or would be so sold if it were mature or if its manufacture, preparation or construction were complete; or

(b) materials such as are used in the manufacture, preparation or construction of any such property as is referred to in paragraph (a) of this definition, and includes any work in progress.

Our definition of stock-in-trade is taken from the United Kingdom Taxes Act 1970. The later equivalent in the United Kingdom of the definition of "stock-in-trade" is to be found in s. 137(4) of the Taxes Act 1970, and the present equivalent s. 100 of the Taxes Act 1988. We may therefore read with profit what the House of Lords had to say about the meaning of the expression "stock-in-trade" in *Reed v. Nova Securities* [1985] STC 124. Lord Templeman speaking for the House said this (at p. 130):

> If a company is to acquire an asset as trading stock, the asset must not only be of a kind which is sold in the ordinary course of the company's trade but must also be **acquired for the purpose of that trade** with a view to re-sale at a profit.
> (Emphasis provided).

In *Rolfe v. Wimpey Waste Management Ltd* [1989] STC 454, CA Dillon LJ said at p. 456 - g, h and a:

> It is not in doubt that land can be circulating capital or a current asset. The obvious instance and indeed the only instance given to us in the course of the argument, is land acquired in the course of business by a property dealer or speculative builder. The land is acquired to be turned into account by building on it and reselling it with the building on it. That apart, however, the general view of the authorities is that expenditure to acquire an interest in land is *prima facie* capital expenditure...

His Lordship then went on to quote Lord Upjohn in another case and added this:

> ... in the field of real property in relation to taxation certain matters are so fundamental as to be axiomatic. Thus in cases **other than those where a man is a property dealer** so that property is his stock in trade it is quite clear that the purchase of a fee simple for a purchase price by a trader is the acquisition of the property for the purpose of a trade and the purchase cannot be regarded as a cost of carrying on the trade. It is therefore capital.
> (Emphasis provided).

After listening to the submissions advanced on behalf of the taxpayer and the revenue, we are of the opinion, that when considered objectively, from the taxpayer's point of view as opposed to that of the developer, the transactions were ambiguous, in other words, their purpose would be open to two interpretations; namely, a commercial purpose or non-commercial purpose depending on how one looks at them. In such a situation, as we have already pointed out, the subjective intention and therefore the motives of the parties are important factors. (See e.g. *Religious Tract and Book Society of Scotland v. Forbes*; *Iswera v. Commissioner of Inland Revenue*, *Rutledge v. IRC* cited above).

Accordingly, it would be convenient if at this stage we turned to consider the next of taxpayer's grounds of appeals which are closely linked to the present ground and which revolves around the question whether in entering into the transactions with the developer the taxpayer was forced to do so with the result that this negatived any intention to trade or to engage in an adventure in the nature of trade.

The circumstances necessitating the relevant transactions; the contention of forced sale

It was contended for the taxpayer that the Special Commissioners had erred in law in finding that the sale of the 407 lots and the 41 lots (which could not be resold by the developer) to the developer, constituted a trading venture notwithstanding that it was a forced sale under conditions of financial stress and business incompetence in housing development, and that notwithstanding that, according to the general law, and also the law on income tax, sale must be consensual and of one's own free will before the proceeds can be chargeable to income tax.

As we have said, the contention of the taxpayer is that a forced sale cannot constitute a sale the proceeds of which are subject to tax because the element of compulsion vitiates the intention to trade.

The circumstances necessitating the realisation of an asset may be of prime importance as it may afford an explanation for the realisation that negatives the idea that any plan of dealing motivated the original purchase.

Thus, in *West v. Phillips* [1958] 38 TC 203 a builder had built some houses with a view to holding them as an investment and some for resale, the latter only being originally treated as part of his trade. Subsequently, however, he decided to sell the others and did so with the aid

of the same organisation which sold his trading houses. It was held by the Court of Appeal, reversing the Commissioners, that he had decided to sell the investment houses for reasons unconnected with his trade; namely, rent control legislation, the rising cost of repairs and increased taxation and so the investment remained outside the scope of his trading activity and their sale at a gain did not give rise to a trading profit.

Another case which illustrates how important the circumstances necessitating the realisation of an asset, is *Dunn Trust Ltd. v. Williams* [1950] 31 TC 477, where it was held that the profit accruing from a sale of shares by a trading company was not derived from a trading transaction.

In giving its reasons for that decision the Court said this:

> The purpose (for which the shares were sold) are quite inconsistent with the purposes that should animate those who direct the fortunes of trading company when they are effecting sales of that company's stock in trade... because the securities were not disposed of in the ordinary course of business or because they thought it would produce a desirable profit or because they thought it was a trading transaction which was financially beneficial to the company.

The case of *Page v. Pogson* [1954] 35 TC 545 also shows the importance of the reason for the sale. There the taxpayer was held not taxable on the profits derived from the sale of one of his two bungalows, the sale having been necessitated by his being offered a position elsewhere.

We note that the Special Commissioners did make the concession that as regards the disposal of the 41 lots and the 407 lots to the developer there was some element of forced selling. This is how they put it:

> ... There was some element of 'forced' selling of the subject lots in dispute due to the lack of member-purchasers acquiring them but there was no reason for us not to construe the final agreement as, *inter alia*, a sale and purchase agreement in which the appellant sold its 407 lots at a price of RM0.25 per sq. ft. to the developer and, as a result of the mutual release of each other's rights and obligations under the previous agreements entered into by both parties, the 41 lots (which had been sold earlier to the developer, *vide* supplementary agreement (D), subject to the developer reselling them to the appellant's members at the same price it purchased from the appellant) were retained by the developer to do what it pleased with them (see para (xxvi) of our findings of fact).

And, further down, on the same page at col 2 para 3, they did make a further concession as follows:

> We are fully aware that the object of the appellant in acquiring the land was to develop it and to sell the lots to its members but because of circumstances beyond its control it could not sell all the lots to its members and hence had to sell the subject lots in dispute to a non-member i.e. the developer.

But they qualified this by adding:

> But we are of the view that the change of 'customers' was of no importance, for it did not change the colour of its transactions, namely, sale and purchase transactions which constituted trading in land within the meaning of s. 4(a) of the Act.

The Special Commissioners also, noted, quite correctly, that "it was the disposal of the 407 lots to the developer and the retention of the 41 lots by the developer that gave rise to the dispute between the taxpayer and the revenue."

We consider that for all practical purposes the taxpayer had no choice but to sell to the developer in view of the predicament in which it found itself. The particular circumstances of that predicament may be taken from the facts as found by the Special Commissioners in their case stated and it will be recalled were as follows:

> (xxiii) after the signing of the supplementary agreement (D), demand for houses by the appellant's (the taxpayer) members slackened due to dissatisfaction with the houses erected; in spite of the appellant (the taxpayer) relaxing its rules regarding payment of a deposit before booking for a lot by potential member-purchasers, 41 lots with houses built thereon out of 111 lots were not taken up;
>
> (xxiv) by this time the appellant (the taxpayer) became aware that it had to incur a lot of expenses to carry out its obligations as provided in the agreements; appeals were made to the developer to revise the terms of the agreements but the developer rejected such appeals;
>
> (xxv) the developer informed the appellant (the taxpayer) that since the appellant (the taxpayer) could not get purchasers for the remaining 41 houses, the appellant (the taxpayer) had to construct the infrastructure which the appellant (the taxpayer)

was obliged to do...; the appellant estimated the cost to be another RM100,000; relations between the parties became strained;

We consider that the sale in the present case was brought about and necessitated by supervening events; namely, the particular circumstances giving rise to the predicament aforesaid and the inability of the taxpayer to raise funds from banks or financial institutions to finance its housing project of which the beneficiaries were its members.

The finding of the Special Commissioners that "there was **some element of 'forced' selling** of subject lots, "and the further finding that" **the object of the appellant** (the taxpayer) in acquiring the land was to develop it and sell the lots to its members but because of **circumstances beyond its control** it could not sell all the lots to its members and hence **had to sell** the subject lots in dispute to a non-member i.e. the developer", (emphasis provided) were findings which were amply justified by the evidence.

Unfortunately, however, the Special Commissioners failed to recognise **the significance** of these findings in the context of the taxpayer's contention that a forced sale cannot constitute a sale the proceeds of which are subject to tax because the element of compulsion vitiates the intention to trade. Indeed, nowhere in their case stated did they direct their attention to the question of intention to trade but instead adopted the oversimplistic approach that although the taxpayer had to sell the lots concerned to the developer, this merely indicated "a change of customers" which was of "no importance for it did not change the colour of the transactions which constituted trading in land within the meaning of s. 4(a) of the Act". Clearly, therefore, the Special Commissioners overlooked the salutary words of Lord Wilberforce in *Simmons v. IRC* [1980] STC 350 at 352 that "trading requires an intention to trade" and that, therefore, the state of mind of those in control of the taxpayer society and their motives were most material.

It is manifestly clear that the dominant purpose and also the dominant motive of the taxpayer was not to make a profit out of the transactions with the developer but to provide a roof over the heads of its members and so, the resulting profit could not have been derived from a trading transaction or an adventure in the nature of trade but was an accretion to capital not liable to tax.

In consequence, the Special Commissioners "misdirected themselves by reaching conclusions inconsistent with primary facts found by them and drew inferences from matters which were of no probative value in supporting their conclusions". (per Lord Oliver in *Lim Foo Yong Sdn. Bhd. v. Director General of Inland Revenue (ibid)* at p. 169 col. 2 F to H).

It follows, that we also uphold the second branch of the taxpayer's argument regarding this part of the case, namely, that by reason of the supervening events aforesaid, it was the developer alone who was the participant in the trading and not the taxpayer who in desperation handed over the project to the developer.

Furthermore, the principle enunciated in *Ransome v. Higgs,* that a person cannot be trading when he merely "procures" someone to trade, applies. Higgs, a taxpayer, did not know what he was doing because he merely "procured" his tax advisors to embark upon a tax avoidance scheme which he did not comprehend. It was held, although the operation resulted in profits and Higgs was amongst others a possible beneficiary, the "procuring" was not trading.

Accordingly, we must answer the broad question, namely, whether the Special Commissioners were entitled to arrive at the conclusion at which they did, in favour of the taxpayer, that is to say, in the negative. It follows, therefore, that we must also answer the specific question of critical substance posed above, in favour of the taxpayer. On this ground alone the appeal must succeed.

The taxpayer's alternative contention: Primary and subsidiary purpose of taxpayer

We must next consider yet another ground of the taxpayer's appeal which was, if at all, there was a trading element in the relevant transactions on the part of the taxpayer, it was at its highest, subsidiary to the primary purpose of providing houses for its members not for a profit but for providing a roof over their heads; it was clearly a capital investment and so there was in law no trading venture. This ground of appeal overlaps, to some extent, the ground of appeal we have just dealt with and therefore, some degree of repetition will be inevitable.

In considering this ground of appeal, we must repeat, that the Special Commissioners had in their case stated made the concession, by way of a finding of fact, that the primary purpose or intention of the taxpayer was to develop the acquired land, being Lot 8265, and to build dwelling houses for its members. (See para 8(vii) of the case stated; p. 27 - C of the Appeal Record). Such a finding presupposes that the land was acquired not for the purpose of re-sale at a profit but as a capital asset. The finding of primary purpose also presupposes a subsidiary purpose.

Where there is a conflict of such purposes, guidance is afforded by cases such as the Privy Council case of *Iswera* (cited above) and *Kirkham v. Williams* [1991] STC 342 as to the proper approach which the Courts should adopt.

In *Iswera,* the facts of which we have already recited, the Privy Council in holding in favour of the revenue that the profit was derived from a trading transaction laid considerable stress upon the fact that the appellant's dominant motive was to make a profit.

In *Kirkham,* one of the appellant's grounds of appeal was that the Commissioner's conclusions that the purchase, the development and sale of the site concerned was an adventure in the nature of trade was inconsistent with their finding of fact that the site was acquired principally to provide for office accommodation and storage space i.e. as a capital asset.

We would add, that in *Kirkham,* as in the present case, the Commissioners had made inconsistent findings and had assumed - quite incorrectly - that every disposal of an asset resulting in a gain, would be in the nature of trading income. The Court of Appeal, by a majority, allowed the taxpayer's appeal.

Applying the principles aforesaid to the present case, we would hold that if, contrary to our primary view, there was a trading element in the relevant transactions on the part of the taxpayer, then the taxpayer's primary purpose or object would be a very material factor when weighing the total effect of all circumstances.

The Special Commissioners having themselves found as a fact that the primary purpose or intention of the taxpayer was to develop the acquired land and to build houses thereon for its members, it is clear that considerable stress should be laid on the taxpayer's dominant motive in entering into the relevant transactions with the developer since motive is linked to purpose. (*Iswera's* case *ibid* at p. 668). If this is done the inevitable conclusion must be that the taxpayer's dominant motive was **not** to make a profit but to fulfil its primary purpose of providing homes for its members. And, lest it be forgotten the taxpayer was a housing society.

Accordingly, the gains accruing to the taxpayer from these transactions were not profits of a trade but merely accretions to capital. On this further ground also the appeal must succeed.

Para 12 Schedule 6 to the Act

In giving their reasons for decision in the case stated, the Special Commissioners said this:

> Finally the exemption given to the appellant for the years of assessment... · by virtue of the then para 12(a) of Schedule 6 to the Act itself envisages **trading or business** transactions between the appellant and its members, for otherwise the provisions of that paragraph would be superfluous to put it another way, there will be no necessity for para 12(a) if trading between a society and its members cannot or does not exist.

There are certain general observations we should like to make concerning Para 12 of Schedule 6.

The reason for the enactment of Para 12 of Schedule 6 is clear and it is this: a co-operative society may at the same time engage in dealings which are mutual as well as business that is not. Where its business dealings result in a profit which is income, liability to income tax arises, subject to the right of a co-operative society to claim exemption under Para 12 Schedule 6 for the first five years of its trading or business dealings. In other words, there must be liability to income tax first and then only the question of claiming exemption under Para 12 Schedule 6 arises. This reminds us of Lord Macnaghten's lambent statement in *London County Council v. A-G* [1901] AC 26, at 35 that "Income tax, if I may be pardoned for saying so, is a tax on income".

If therefore, the taxpayer in this case is correct in its contention that arising from its transactions with the developer it had received not income within the meaning of s. 4(a) of the Act, but a capital profit or merely accretions to capital, not liable to be brought into the computation of income tax, - and, indeed we have so

held - recourse to para 12 Schedule 6 would be wholly unnecessary.

We need hardly add that the taxpayer here was not at all relying on Para 12 to Schedule 6; and rightly so, for this provision is of no direct relevance to the issues which arise for decision in this appeal.

Consequently, the fact that the taxpayer had been granted exemption by virtue of Para 12(a) of Schedule 6 to the Act in respect of its income for the years of assessment 1969, 1970, 1971 and 1973 was of no relevance to the questions arising for decision in this appeal which concerned the years of assessment 1972 and 1974.

The mutuality point

A separate ground of appeal was argued before us based upon the doctrine of mutuality which it was contended applied to the taxpayer.

In view, however, of our having upheld the other contentions of the taxpayer, which we have considered and discussed above, we do not consider it necessary to rule on this separate ground since, should we do so, it would be merely *obiter*.

Summary of Conclusions

To summarise, the conclusions expressed above are as follows:

(1) The finding of the Special Commissioners that the taxpayer's primary object in the purchase of the land was to develop the land, build houses thereon and sell them to members so that the taxpayer's objective of enabling each member to have a roof over his head, was amply justified by the evidence.

(2) Consequently, the Special Commissioners subsequent conclusion that the land since the date of acquisition had never been treated or held as an investment, on the contrary, it was held as stock in trade throughout, was wholly inconsistent with their earlier finding and contrary to the evidence.

(3) Accordingly, the Special Commissioners had misdirected themselves in law by reaching conclusions inconsistent with the primary facts found by them and drew inferences from matters which were of no probative value in supporting their conclusions. (See *Lim Foo Yong Sdn. Bhd. v. Director of Inland Revenue* [1986] 2 MLJ 161 at 169 col. 2 f to h per Lord Diplock).

(4) In so far as the relevant transactions between the taxpayer and the developer were concerned, there was no trading on the part of the taxpayer or any adventure in the nature of trade, although undoubtedly, the developer alone was trading.

(5) Alternatively, if there was a trading element on the part of the taxpayer as well in those transactions, it was, putting the case for the revenue at its highest, subsidiary to the principal purpose of providing a roof over the heads of each of its members, and so, in disposing of the lots concerned to the developer, the taxpayer had merely realised a capital asset whose value he had enhanced by subdivision and the issue of separate titles, and it was, therefore, not taxable on the profits realised thereby as they were merely accretions to capital (See *Kirkham v. Williams (ibid)*).

In all the circumstances, we would allow the appeal, set aside the judgment of the Court below and discharge the assessments. Costs at all levels to the taxpayer. Deposit to be refunded to the taxpayer.